MULTIMEDIA UNIVERSITY

STUDENT ID NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 1, 2015 / 2016 SESSION

BFN3104 – CORPORATE FINANCIAL STRATEGIES

(All Sections / Groups)

16 OCTOBER 2015
9.00 A.M – 11.00 A.M.
(2 Hours)

INSTRUCTIONS TO STUDENT

1. This Question paper consists of 2 pages with **7** questions.
2. Answer **ALL** questions and the distribution of the marks for each question is given.
3. Please write all your answers in the **Answer Book** provided.

Students are not allowed to take this paper out of the examination hall/room.

Question 1 (10 marks)

Describe the product life cycle (***PLC***) and explain its developmental stages with a graphical example. (10 marks)

Question 2 (19 marks)

a. Your friend tells you about an arbitrage opportunity. You can buy stock for RM25 in Taiping and sell it for RM25.15 in Newark. You have RM50,000 available for one day that is earning nothing so you jump on the opportunity and immediate begin selling and buying 1,000 shares. In the process, you discover that it costs you RM0.06 per share to buy in Taiping and RM0.05 per share to sell in Newark. There are additional expenses of RM0.04 per share for such things as transfer and communications costs. You need to spend two hours of your work time where your opportunity cost is RM20 per hour. Have you made money on this "arbitrage" opportunity? (15 marks)

b. Give two examples of announcements that are anticipated. (4 marks)

Question 3 (15 marks)

a. Your business has experienced some financial distress. Your assets have an equal chance of being worth either RM1,600 or RM800 at year's end. Your debt is RM1,000 and due at the end of the year. Now suppose you substitute your current assets for riskier assets that have the same expected value but a wider dispersion. The riskier assets now have equally likely payoffs of RM1,800 and RM600. With the same expected value, the asset substitution renders a zero NPV. Does this mean that the debtholders are just as well off? (8 marks)

b. What is asset substitution and underinvestment? (4 marks)

c. What is an optimal contract? (3 marks)

Question 4 (15 marks)

Abu Homebuilding and Beh's Homebuilding will merge. Abu has a total market value (V_A) of RM40M (M = million), and Beh's has a total market value (V_B) of RM25M. Their merger will lead to operating efficiencies and will produce a present value savings of RM6M.

Answer the questions below:

i. Ignore expenses and the payment of a premium. What is the total market value of the merged firms? (4 marks)

ii. Ignore the payment of a premium. If the merger would entail expenses (E) amounting to RM4M, is there a net advantage to merging (NAM)? (5 marks)

iii. If Abu buys Beh's outstanding shares, paying Beh's common stockholders a RM4M premium, will the acquisition be advantageous to Abu's shareholders? (5 marks)

iv. Who if anyone gains and loses in this merger? To what can any gains or losses be attributed to? (3 marks)

Continued...

Question 5 (7 marks)

a. What is a derivative? (2 marks)

b. What are the possible benefits derive from hedging by a multinational company? (5 marks)

Question 6 (17 marks)

a. Consider the following projects (data in thousands RM):

Project	A	B	C	D	E	F	G
Initial Cost	10	20	20	15	30	40	20
NPV	11	36	8	16	40	30	14

Calculate the ***profitability index*** **(PI)** for the projects. Find three projects with the ***lowest*** PIs that have a total initial cost of RM80,000 with a collective NPV of RM52,000. (13 marks)

b. You are evaluating a proposed expansion project and you determine that the DCF-NPV is −RM50,000 (negative). You think you might have a future growth option to expand further but it would cost you an additional RM100,000 (in today's ringgits) to have this option. If this future opportunity occurs, you estimate the present value of this option will be RM250,000. However, there's only a 50 percent chance of this occurring. Does the growth option make investment in the proposed project a positive NPV? (4 marks)

Question 7 (17 marks)

a. The firm you work for is trying to decide to file either a Chapter 7 or a Chapter 11 bankruptcy. If it chooses to reorganize, the following future cash flows (M = millions) are expected:

Year	1	2	3	4	5
CF (M)	RM20	RM40	RM60	RM70	RM90

The appropriate discount rate is 15 percent. The liquidation value of the firm is RM200M (Assuming you are now working in the United States of America).

Answer the questions below.

i. What is the reorganization value? (7 marks)

ii. Should the firm file a Chapter 7 or a Chapter 11 bankruptcy? (2 marks)

b. Suppose a firm's financial statements indicate the following financial ratio values: $X_1 = 15\%$, $X_2 = 30\%$, $X_3 = 17\%$, $X_4 = 20\%$, and $X_5 = 2.0$ (8 marks)

Answer the below questions.

i. Calculate the Z-score using the Altman model:
$$Z = 0.012(X_1) + 0.014(X_2) + 0.033(X_3) + 0.006(X_4) + 0.999(X_5).$$

ii. Is the firm likely to go bankrupt within one year?

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